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SUBCOMMITTEE ON INVESTIGATIONS AND OVERSIGHT

OF THE

COMMITTEE ON PUBLIC WORKS AND TRANSPORTATION U.S. HOUSE OF REPRESENTATIVES

ON THE

IMPROVEMENT NEEDED IN THE IMPLEMENTATION OF THE UNITED STATES INTERNATIONAL AVIATION POLICY

(Based on hearings by the Subcommittee on Investigations and Oversight, July 28, 29, 30; August 4; October 20; December 9 and 10, 1981; and April 21 and May 18, 1982)

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LETTER OF TRANSMITTAL

WASHINGTON, D.C., *August 8, 1983.*

Hon. JAMES J. HOWARD,
Chairman, Committee on Public Works and Transportation, U.S. House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: The Subcommittee on Investigations and Oversight undertook an extensive and exhaustive review of the implementation of the International Aviation Policy of the United States over a period of many months, covering both sessions of the 97th Congress.

I am pleased to forward to you the attached report which summarizes the results of that effort and contains the Subcommittee's conclusions and recommendations for improvement.

I believe you will find this effort to be thoughtful, objective, and a full and fair analysis of the issues. It should be a very useful document to the Committee on Public Works and Transportation, the Congress, and those departments of the Executive Branch of the U.S. Government which have responsibility in these matters.

With best wishes, I am,

Very truly yours,

ELLIOTT H. LEVITAS,
Chairman, Subcommittee on Investigations and Oversight.

FOREWORD

The success or failure of United States air carriers in international operation is measured by the manner in which the international aviation policy of the United States is implemented throughout the world. That policy was set forth in the 1979 International Air Transportation Competition Act.

The Public Works and Transportation Committee has a vital interest and concern to insure that the governmental bodies which share responsibility in carrying out the intent of the Congress, as specifically set forth in that legislation, adhere to that policy.

The Subcommittee on Investigations and Oversight has inquired into all phases of the implementation of that policy and has prepared this report as a guide to future efforts.

I believe this document will prove to be beneficial to the Committee, and certainly, there should be no question of its usefulness to all governmental agencies and parties interested in international aviation matters.

JAMES J. HOWARD,
Chairman, Committee on Public Works and Transportation.

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Introduction

The 1979 International Air Transportation Competition Act (IATCA) presents a balanced set of international air goals, including strengthening the competitive position of international air carriers and eliminating discriminatory and unfair practices encountered by U.S. carriers in foreign countries.

In actual practice, however, our international carriers believe that implementation of governmental policies—including the open skies policy initiated in 1978—has resulted in an unbalanced emphasis on consumer and foreign interests, including the condoning of foreign discriminatory practices, at the expense of U.S. airline revenues.

Our hearings were designed to explore the consistency of these governmental goals with the goals established by the legislation.

U.S. international air carriers have been reporting continuing severe financial losses, with operating deficits of $200 million in 1980. During the first three months of 1981, the U.S. air carriers showed even greater losses in their international operations—$125 million.

However, it should be noted that carriers of other countries are also reported to be losing money. During 1980, International Air Transport Association (IATA) air carriers reported deficits of over $5 billion. A number of factors have contributed to the problems of all carriers, including sluggish economies and increased fuel costs. For the U.S. carriers, some additional factors exist which do not appear to affect other carriers. For instance, they are unable to get low-interest loans needed to modernize their fleets, and they encounter unfair and discriminatory practices by foreign governments. Unfair and discriminatory practices, to the extent measurable in dollar terms, have been estimated at $20 to $25 million a year in lost earnings.

Since 1978, U.S. international aviation policy has been described as open policy, pro-competition, and pro-consumer. Inspired by the philosophy of the economics of free market competition, the U.S. government has expanded its policies towards increased deregulation—both in the domestic and international markets. The change in policy, initiated by the Carter Administration, impacts on the airlines, travelers, and international relations.

Implementation of international aviation policy is in the hands of three agencies: Civil Aeronautics Board (CAB), Department of Transportation, and Department of State. The CAB, which is now destined to "sunset" in 1984, provides expertise in economic analysis and regulates the air industry. The Department of Transportation is responsible for providing international aviation policy guidance. The Department of State has the lead role in coordinating and developing positions, strategies, and procedures for international negotiations, and generally chairs interagency negotiating meetings.

There has been criticism of the pro-competitive policy, and particularly its implementation in the international arena. There has also

been continued criticism of the lack of a firm U.S. response to unfair and discriminatory practices of most foreign governments. Nine days of hearings were held by this Subcommittee to explore the many facets of these important issues. We felt the need to reevaluate our policies and to identify problems and their possible solutions.

Testimonies received during the hearing included the following:

General Accounting Office.—To document their findings of unfair and discriminatory practices by foreign governments against U.S. airlines.

Witness: Frank Conahan, Director of the International Division.

Airlines.—Major airlines in the field and hopeful new entrants gave us their experiences and their opinions.

Witnesses:

C. E. Meyer, President and Chief Executive Officer, Trans-World Airlines, Inc.

John J. Casey, President and Chief Executive Officer, Braniff International.

William T. Seawell, Chairman of the Board and Chief Executive Officer, Pan American World Airways, Inc.

William A. Kutzke, Vice President, Northwest Airlines, Inc.

Thomas F. Grojean, President, Flying Tiger Line, Inc.

Monte Lazarus, Senior Vice President for External Affairs, United Airlines.

Prior administration officials.—To provide us with information on their involvement in policy formulation and implementation.

Witnesses:

Secor D. Browne, Former Chairman, Civil Aeronautics Board.

Alfred Kahn, Former Chairman of the Civil Aeronautics Board and Economic Adviser to President Carter.

Marvin Cohen, Former Chairman of the Civil Aeronautics Board.

Brock Adams, Former Secretary, Department of Transportation.

Officials of the Reagan administration.—To provide information on current policy and process for implementation.

Witnesses:

Dan McKinnon, Chairman, Civil Aeronautics Board.

Darrell M. Trent, Deputy Secretary, Department of Transportation.

Judith Connor, Assistant Secretary for Policy and International Affairs, Department of Transportation.

Robert Hormats, Assistant Secretary for Economic and Business Affairs, Department of State.

William E. Brock, Ambassador and U.S. Trade Representative.

Other expert witnesses.—To provide us a broader perspective on the issue.

Witnesses:

Knut Hammarskjold, Director General, International Air Transport Association.

Ron Danielian, Executive Vice President and Treasurer, International Economic Policy Association.

Donald C. Comlish, Vice President for International Affairs, Air Transport Assocation of America.

Edward J. Driscoll, President and Chief Executive Officer, National Air Transport Association.

We believe that these hearings have been the clearest focus by Congress on this area of commercial activity. The primary problems we have identified are:

Weaknesses in the bilateral negotiation process.

Unequal trading of rights in negotiations.

U.S. policies weakening the international air fare structure.

U.S.-unsupported carriers vs. government-supported foreign carriers.

Lack of firm U.S. response to unfair or discriminatory practices by foreign governments.

We have summarized our findings in this report for the full committee. The first section of the report provides a short background on international aviation policy. Section II centers on the problems in carrying out IATCA policies as they surfaced during the hearings. Section III contains the Subcommittee's conclusions and its recommendations for improvement.

I. Background

Bilaterals are negotiated agreements between any two countries that serve to distribute international rights in air transportation. Such agreements establish the routes, rates, and other air transport conditions between the two countries. "Third-party" countries are sometimes able to obtain limited access to those routes, when they can demonstrate strong connection to their own markets—this is called "Fifth Freedom" or "Beyond" rights. Bilaterals have remained the principal system for negotiating international air rights since they were first established by the Bermuda I Conference of 1946.

In this same Conference, the International Air Transport Association (IATA), an association representing international airlines, was given the responsibility for developing international air fares and tariffs on a world-wide basis. The IATA fares are submitted to the pertinent governments for approval, and when obtained, the fares are incorporated into the various bilateral agreements when negotiated. This fare-setting process has remained in effect since 1946 and it constitutes the only multilateral component of international air policy. In the United States, the Civil Aeronautics Board has the responsibility of reviewing and approving IATA-developed fares.

The first real attempt to make major structural changes in international air policy came with the Carter Administration's "open skies" policy. In the process of deregulating domestic air transportation, it was decided to also deregulate international air transportation. In 1978, the CAB—after 33 years of approving IATA rates—issued an order directing IATA to "show cause" why CAB should not rule that IATA tariff agreements are no longer in the public interest, and, therefore, should not be approved. This represented a unilateral proposal by CAB to withdraw from IATA, and it caused a generally negative reaction from the international community. As the other "prong" of open skies for international air, the Administration negotiated a series of more liberal bilateral agreements with other countries which gave foreign governments new access to interior gateways in the U.S. in exchange for flexible fares and the addition of new U.S. carriers.

Prior to 1977 all the IATA member carriers flying the North Atlantic routes charged the same fare for any given market in accordance with fare agreements developed in area traffic conferences. The North Atlantic Traffic Conference's jurisdiction stretched from England to the Middle East. All fares had to receive a unanimous vote of Conference members even if a carrier did not fly in that market segment. By 1977, when the open skies competitive policy of the United States was initiated, IATA was having difficulties getting approval of its fares both by its membership and the CAB. This situation forced IATA to reevaluate its own procedures. This resulted in some relaxation of IATA's regulations. The unanimity rule was replaced by a simple majority vote. Special innovative fares were introduced as a replacement for a single set of fares. IATA also developed a two tier membership plan: one tier would allow a carrier to participate only in the trade functions of IATA; the other would allow a carrier to participate in both trade functions and tariff conferences.

The 1977 through 1982 period saw a significant realignment in the fundamental approach to international aviation. It saw the loosening of bilateral agreements as a result of the Bermuda II agreement, the start of Laker Airlines Skytrain low fare service across the North Atlantic, some relaxation in the standard way of setting international aviation tariffs thru IATA, and the development of a new approach to setting fares which would permit a level of competitive pricing in an international arena which has not been traditionally competitive—European Civil Aviation Conference agreements (ECAC).

The U.S. policy during this period has been to remove the previous constraints which hindered a free competitive environment. The Carter Administration and the CAB used all available instruments to eliminate restraints on the market place. The 1978 CAB IATA Show-Cause Order would have removed the antitrust immunities which CAB had historically granted U.S. carriers to participate in the IATA tariff conferences. The scope of the order was subsequently reduced in scope to the North Atlantic Traffic Conference—a Conference whose market includes the most densely travelled routes in the world. This order was scheduled to become effective in September 1981. However, as a result of this Subcommittee's oversight hearings, changes governing the regulation of IATA giving more competitive flexibility to carriers, and the progress being made within ECAC toward an agreement to promote competitive fares, Congressman Elliott H. Levitas (D–GA) offered the "Levitas Amendment" to the FY 82 DOT Appropriation Bill. This Amendment would postpone for one year the effective date of the IATA Show-Cause Order of the CAB. The Underlying purpose would be to point out to those involved in ECAC negotiations the potential consequences of failure to achieve a more competitive pricing system on the North Atlantic. The net effect of these events was that in July 1982 a six months interim agreement was reached. This agreement was recently extended to October 1983 at which time it will be further evaluated. The ECAC agreement is a multilateral agreement in principle and a bilateral agreement in the specifics such as the reference fares and the zones of flexibility.

II. Problems Carrying Out IATCA Policies

The underlying philosophy behind current U.S. aviation policy, as enunciated by the Congress, is the creation of a transportation system based on competition that achieves a wide variety of services and price options for the consumers while assuring the competitive position of our international air carriers. IATCA lists the goals for international aviation policy as the following:

"(1) the strengthening of the competitive position of United States air carriers to at least assure equality with foreign air carriers, including the attainment of opportunities for United States air carriers to maintain and increase their profitability, in foreign air transportation;

"(2) freedom of air carriers and foreign air carriers to offer fares and rates which correspond with consumer demand;

"(3) the fewest possible restrictions on charter air transportation;

"(4) the maximum degree of multiple and permissive international authority for United States air carriers so that they will be able to respond quickly to shifts in market demand;

"(5) the elimination of operational and marketing restrictions to the greatest extent possible;

"(6) the integration of domestic and international air transportation;

"(7) an increase in the number of nonstop United States gateway cities;

"(8) opportunities for carriers of foreign countries to increase their access to United States points if exchanged for benefits of similar magnitude for United States carriers or the traveling public with permanent linkage between rights granted and rights given away;

"(9) the elimination of discrimination and unfair competitive practices faced by United States airlines in foreign air transportation, including excessive landing and user fees, unreasonable ground handling requirements, undue restrictions on operations, prohibitions against change of gauge, and similar restrictive practices; and

"(10) the promotion, encouragement, and development of civil aeronautics and a viable, privately owned United States air transport industry."

This section describes the alleged problems in the implementation of these objectives since the late 1970's. In particular, we shall examine whether U.S. procompetitive policies in international air travel, and overall lack of U.S. priority placed thereon, have resulted in a weakening of the economic position of our international air carriers. In terms of legislative oversight, we shall review whether goals 1.9, and 10 of IATCA, concerned with economic health and a fair market environment for our carriers, have been sacrificed in pursuit of the other goals.

Weaknesses in the Bilateral Negotiation Process

International air policy is carried out by three agencies: the Civil Aeronautics Board (CAB), Department of Transportation, and Department of State. Negotiations on routes and frequency of air service between countries are usually bilaterally negotiated. The negotia-

tions on behalf of the airlines and the traveling public are conducted by a U.S. negotiating team representing the three agencies. The chairman of the team is designated through a consultative process among the agency officials, although the Deputy Secretary of State who handles aviation normally has the lead. Carriers do not participate in international negotiations. Rather, their interests are represented at the negotiations by the Air Transport Association (ATA) and the National Air Carrier Association (NACA). ATA and NACA act as observers at the negotiations and report progress back to their member carriers. Foreign governments—who, unlike the United States, typically have one carrier per country—include industry representatives as participants in their negotiations.

Former Secretary of Transportation Brock Adams stressed the need to negotiate aviation agreements at a very high level. Some foreign countries have a Minister of Transportation, or equivalent, and a highly skilled team of experts at negotiations. His experience has shown that the U.S. team comes from different places in government, with some not having the necessary expertise. While he was in the Department of Transportation, he could never obtain assurances from State that an Assistant Secretary of State would carry on negotiations when the United States had substantial problems. If we work with bilaterals, he suggested that we need (1) a single point within the U.S. Government that handles the treaty negotiations, and (2) long-term expertise and knowledge. He believed that the function should be transferred to the Department of Transportation, and assigned to an Assistant Secretary, who has regular responsibility for it.

U.S. Trade Ambassador William Brock also believed that the Department of Transportation should be assigned the responsibility for international aviation because it has extensive experience. He stated that the issue should also be placed in the context of the General Agreement on Tariffs and Trade (GATT). GATT deals with multilateral type negotiations that concern the establishment of principles to guide trade relationships and has dispute settlement mechanisms.

Former CAB Chairman Alfred Kahn believed that the lead responsibility for international aviation should be assigned to the Department of State because (1) aviation is part of international commerce of goods and services; (2) State would be less responsive than Transportation to private interests; and (3) specialists in Transportation tend to be cartelists who don't trust free competition.

UNEQUAL TRADING OF RIGHTS IN NEGOTIATIONS

To promote competition, the Executive (primarily under the Carter Administration) negotiated bilateral agreements with other governments that increased the frequency of air service between the U.S. and other countries. In addition, more U.S. gateways were opened to foreign carriers, and new U.S. entrants were granted permission to enter the market. By increasing competition, it is argued, the traveling public would be better served, fares would come down, and airlines would need to become more efficient in order to stay in business. Further, U.S. carriers' participation in IATA should be reduced or avoided in order to allow this type of competition to take place.

One example frequently cited is the bilateral agreement negotiated between the United States and the Netherlands involving KLM, Royal Dutch Airlines. Prior to the implementation of the agreement, KLM operated 26 wide-bodied flights per week to three U.S. gateways: Chicago, Houston, and New York. In August 1981, after the agreement, KLM was operating 36 wide-bodied flights per week to five U.S. gateways: Chicago, Houston, New York, Atlanta, and Los Angeles. At the same time, only two of the more than 12 U.S. passenger airlines authorized by the CAB to serve the Netherlands were actually flying to Amsterdam. Within Europe, KLM has a significant market due to its beyond rights capabilities (i.e., its rights to fly passengers to a large number of cities in Europe beyond Amsterdam) and its pooling arrangements with airlines of other European countries. Within the United States, an international carrier transports passengers from various parts of the country to the gateway cities to fly to Europe. By increasing the number of gateway cities granted to KLM, and the airline's ability to fly passengers from the United States to cities throughout Europe, KLM has a significant advantage.

Representatives of the major U.S. carriers expressed a strong concern that bilateral agreements be negotiated only when access to lucrative markets can be traded for equally valuable economic foreign markets and beyond rights. Their opinion is that U.S. carriers are among the most efficient in the world. However, if U.S. carriers are forced out of the competition in the long term, consumers would be in the hands of the foreign carriers, who would likely raise fares.

The Subcommittee is pleased to have noted that the attitude of U.S. negotiators at bilateral conferences seemed to have hardened since the beginning of our hearings in July 1981 in that they don't seem to give away rights for the sake of having a treaty. In addition, changes have included (1) shifts in personnel heading up the agencies playing a role in international air transportation, (2) installation of a new CAB chairman, and (3) the dropout of two major international carriers (Braniff and Laker).

COSTS OF ADDING NEW U.S. ENTRANTS

The U.S. Government's procompetitive international policy also promotes the entry of additional airlines into the market. Prospective new U.S. entrants to the market expressed concern to this Subcommittee that the United States will revert to its more restrictive policies, prior to open skies. Administration officials likewise indicated that the major airlines were interested in minimizing competition—and therefore increased fares. Such smaller airlines as Air Florida and World Airways should be encouraged to enter the international market, as well as such major domestic carriers as United and Eastern.

Representatives of the major airlines (as Trans World, Braniff, and Pan Am) testified that they did not want to keep additional entrants out of the market. However, they do point out that whatever problems exist for them—as discriminatory and unfair practices—will likewise exist for the new entrants. In addition, they question the "worth" to the total system of adding additional U.S. carriers in the same markets. Too often, carriers compete against each other. The new carriers

have, for the most part, been limited, "cream-skimming" operations in a few large markets, similar to charter operations. They do not provide an international transportation network, but may start a new operation and then abandon it if it is not lucrative. When they drop out of the market, they are likely to leave unused routes and authority. What are the added competition and unused rights worth to the United States?

Department of Transportation appointees seeemed to generally agree with the positions taken by the incumbent airlines in questioning whether there's a need for additional capacity and what price the U.S. government is paying in trading routes to get new entrants in the market.

Former Secretary Brock Adams indicated that new entrants usually provide point-to-point service (i.e., they don't fly a system through a portion of the world so passengers can get on a plane and easily go from one country to another). They provide a service wherever there's a good market. If they don't do well in that market, they pull out. If they knock out another American carrier before they pull out, they leave the field open to a foreign carrier.

Judith Connor, a representative of the current administration, pointed out that when we introduce new carriers in the market, they may end up competing among themselves or with the incumbent carriers. The overall size of the traffic pie increases with additional services and lower fares. However, the pie may not increase enough to give any one carrier a large enough slice to produce profitable operations. The introduction of new entrants may become an empty victory.

U.S. POLICIES WEAKENING THE INTERNATIONAL AIR FARE STRUCTURE

The International Air Transport Association (IATA) is a trade association with a membership of 113 international airlines. It provides a multilateral forum for members to develop an integrated air transport system and to coordinate airline tariff proposals.

Disagreement in our hearings centered on U.S. airlines' participation in IATA.

Alfred Kahn referred to IATA as a price-fixing cartel. Although bilateral agreements are cumbersome, he felt that it is better to use the principles of free competition than the preference of governments for regulating international fares. IATA, he said, is a fare-setting forum that tends to close out such low-cost, efficient, aggressive airlines as Air Florida and Laker. Kahn sees fare setting through IATA resulting in higher fares than would occur under competition.

The CAB (under Kahn) issued a "show-cause order" in June 1978 regarding antitrust immunity granted to U.S. carriers participating in IATA's rate-setting activities. The Departments of State and Transportation argued in favor of the U.S. carriers; that the order was discriminatory against U.S. carriers and may be counterproductive in the area of foreign relations. CAB revised its order, and limited only U.S. carriers' participation in the North Atlantic IATA Conference.

Knut Hammarskjold, Director General of the International Air Transport Association, testified that U.S. international aviation

policy changed dramatically in 1978. It was not only a major shift from prior policy, but radically different from the policies of other governments. Nations have been troubled by the manner in which U.S. policy has been implemented in the last few years, which he describes as "messianic fervor." The United States has emphasized deregulation and free market in the international sense. (Foreign governments generally disagree with this.) The show-cause order was viewed as a unilateral effort to impose U.S. standards on other nations. Although the CAB eventually modified this order, limiting U.S. airline participation to the U.S.-North Atlantic tariff conferences, the damage was still done. The absence of U.S. carriers from IATA talks for three years has made it impossible to maintain a comprehensible passenger tariff structure.

Former DOT Secretary Brock Adams agreed with Mr. Hammarskjold in criticizing the show-cause order. He does not believe that the United States can export its antitrust laws into the international aviation community. Preventing U.S. airlines from meeting with 90 percent of the world's airlines through IATA, he felt, would be a tragic mistake. International civil aviation is not a free, open market. There are regulations in existence. He does not see IATA, as a price-fixing cartel. If we don't participate in IATA, we must use the bilateral system; which is also a form of government regulation.

U.S. UNSUPPORTED CARRIERS VS. GOVERNMENT-SUPPORTED FOREIGN CARRIERS

Ambassador William Brock, U.S. Trade Representative, gave the following description of the differences in economic support provided to our carriers and that provided to foreign carriers by their governments:

"Foreign governments pour hundreds of millions of dollars into their civil aviation industry. Our government provides U.S. carriers with no financial support. Foreign governments provide their carriers with monopolies covering everything from customs to ground handling to catering. Our government not only does not provide such an advantageous situation, it prohibits it. Where foreign countries have permitted airlines to enter pooling arrangements, we have given our carriers the open skies policy."

If foreign carriers receive subsidies and other forms of economic support, unsubsidized American carriers suffer from an unfair disadvantage. Many foreign carriers are enjoying benefits that are considered illegal in the United States. For instance, a government-controlled carrier can have a vast, interlocking network that includes domestic and international transportation, airport authorities, travel agencies, tourist bureaus, and freight forwarders. They can also benefit from "pooling" arrangements in which carriers of two or more countries mesh their schedules, prices, sales promotions, reservations, and revenues. With pooling arrangements, airlines increase their load factors and split revenues. Other governments are interested in their airlines for such reasons as promotion of tourism, defense capabilities, and projection of national image—not just for purposes of transportation. Witnesses representing U.S. carriers did not request government

subsidies; they mainly requested acknowledgement and backing by the U.S. Government so they can compete on an equal basis.

The positions expressed by the last three chairmen of the CAB are summarized as follows:

Alfred Kahn initially claimed that only the Concorde and Sabena are subsidized by their governments, England and Belgium. He did acknowledge that foreign airlines received such support from their governments as loan guarantees, direct subsidies, low interest rate loans, loans which are forgiven, and Export-Import Bank financing for new aircraft. However, protecting our airlines, as done in the past, is not a logical step. Competition in the real world is imperfect. Competitors are subject to advantages and disadvantages.

Marvin Cohen agreed that foreign airlines do receive subsidies, even though their governments would prefer that their airlines make money. What foreign governments fear is that U.S. carriers would drive them out of business because of U.S. carriers' great efficiency.

Dan McKinnon, the current chairman, agrees that there are foreign air carriers that are government owned or subsidized, but he does not believe that they behave any "differently" from non-subsidized carriers. He said the factors contributing to the decline in the U.S. market share included the introduction of new low fare scheduled services such as Laker, and the change in composition of the traveling public (e.g., fewer Americans, more Europeans traveling). When the total market is down, all airlines—subsidized and non-subsidized—tend to cut capacity.

Representatives of the major U.S. international air carriers again pointed out that virtually every carrier is having economic difficulties. The risk of failure makes government support and subsidy an important difference between the two types of operations. The following example was provided by the airlines to illustrate the preferential treatment provided to foreign carriers:

In 1980, the Export-Import Bank gave $1.7 billion worth of loans to foreign carriers of 27 nations at interest rates ranging from 8 percent to 9.25 percent to purchase new aircraft from U.S. manufacturers. Most of these loans have no payment due for 5–7 years after they receive the money. U.S. airlines are charged loan rates of 20–21 percent; interest tied to the prime rate. Only 10 percent of the aircraft on order are by U.S. carriers; 90 percent are from foreign carriers. Since the United States is the major supporter of the Export-Import Bank, it is thus subsidizing foreign competition against its own carriers.

The Export-Import Bank was established by the Roosevelt Administration to stimulate U.S. exports by providing loans when the borrower could not obtain the funds elsewhere. Loans are, then, provided to foreign carriers to purchase U.S. aircraft. This provides a benefit to our balance of payments and it contributes to lowering aircraft purchase prices by the increased production by U.S. manufacturers. The Ex-Im Bank, however, does not require a carrier to show that it has sufficient traffic potential to warrant a loan, another major disparity with U.S. carriers seeking commercial loans.

U.S. airlines are experiencing aging equipment because of the high cost of aircraft replacement. The U.S. international fleet is 8 years old,

on the average, compared to the foreign carrier fleet average age of 4.6 years. The ability of foreign airlines to purchase new equipment, using subsidized loans, might create a further, long-term disadvantage for the U.S. airlines. As equipment gets older, the U.S. share of the market is also likely to become smaller.

Brock Adams reiterated the concern cited by others about the American fleet getting older. Foreign airlines are purchasing new U.S.-manufactured, fuel-efficient equipment which makes them more competitive with U.S. carriers. As both the U.S. carriers' equipment and systems grow older, the American Carrier System is likely to grow smaller in capacity and be less able to compete. The United States should have a national concern for its carriers, who cannot write off their losses, in seeing that they get a fair deal.

PREVALENCE OF UNFAIR/DISCRIMINATORY PRACTICES

"Whenever the Civil Aeronautics Board, upon complaint or upon its own initiative, determines that a foreign government or instrumentality, including a foreign carrier (1) engages in unjustifiable or unreasonable discriminatory, predatory, or anticompetitive practices against a United States air carrier or (2) imposes unjustifiable or unreasonable restrictions on access of a United States air carrier to foreign markets, the Board may take such action as it deems to be in the public interest to eliminate such practices or restrictions. Such actions may include, but are not limited to, the denial, transfer, alteration, modification, amendment, cancellation, suspension, limitation, or revocation of any foreign air carrier permit or tariff pursuant to the powers of the Board under the Federal Aviation Act of 1958." International Air Transportation Competition Act of 1979, Section 23(b)(1).

Frank Conahan, Director of the International Division of the General Accounting Office, presented testimony on unreasonable user charges and discriminatory practices in international air transportation. The source of GAO's data is a 1978 report dealing with the subject, updated with information obtained from the CAB and U.S. carriers in 1981. Mr. Conahan testified that the basis of the problem is the heavy involvement of foreign governments in international travel. U.S. carriers are privately owned; foreign carriers are either owned or financially supported by their governments; and other objectives than travel are involved.

Some of the unfair user charges and unfair practices frequently cited include:

The landing fees at London's Heathrow Airport are the highest in the world. At Heathrow, all 747's pay the same landing fees, but such fees hit the North Atlantic flights disproportionately. Trans-Atlantic flights from the U.S. arrive in the morning—the time at which the highest rates are charged. British Air, on the other hand, generally flies shorter hauls, uses smaller equipment, and lands at different hours of the day. Whereas a trans-Atlantic 747 flight pays an average of $350 per landing in the United States, the same flight would pay approximately $10,000 at Heathrow. TWA's President C. E. Meyer, Jr., testified that TWA paid $12.4 million in user charges for land-

ing at Heathrow in 1980. William Seawell, President of Pan Am, stated that although American flights counted for less than three percent of Heathrow's operations, they have contributed 9 percent to the airport's revenues.

Japan's noise pollution charge also falls most heavily on 747 aircraft, in spite of the fact that they are quieter than narrow-bodied aircraft. U.S. airlines fly long-hauls using 747's; Japan Airlines, landing at Haneda Airport, more frequently flys short-hauls using narrow-bodied equipment.

Italy has a monopoly over groundhandling operations. Whereas Alitalia can develop and staff its own ticketing and baggage handling operations, U.S. carriers cannot; resulting in customer complaints and airline inefficiencies.

A number of countries—including Bolivia, Canada, Colombia, Ecuador, Japan, Peru, and Venezuela—charge higher fuel prices to U.S. carriers than their national carriers. In Peru, as an example, airlines are charged 50 percent higher prices than the local carrier plus overcharges. Airlines which have an agreement with the Peruvian government are exempt from these overcharges.

Several countries—such as Brazil, Canada, India, Japan, and New Zealand—have restrictions on charter operations.

The countries of Malaysia, Nigeria, the Netherlands, Pakistan, Panama, Peru, Poland, Venezuela, and the USSR have restrictions on flight frequencies, number of carriers, types of aircraft used, and passenger pick-ups.

Pricing restrictions exist in France, Pakistan, Peru, Portugal, and Switzerland.

Strict limitations on cargo are imposed on U.S. carriers by Belgium, Canada, France, Germany, Hong Kong, Italy, Japan, Korea, Mexico, Pakistan, Taiwan, and the United Kingdom.

Unreasonable or discriminatory navigation and other user charges exist in Australia, Bolivia, Brazil, Guatemala, Japan, Mexico, New Zealand, Nigeria, Panama, Paraguay, Peru, Singapore, the United Kingdom, and Yugoslavia.

Currency remittance problems exist all over the world; and especially in Ghana, India, Kenya, Nigeria, Pakistan, and Taiwan. The airline involved either loses use of the money held by the foreign government for some period of time or it has to buy local goods to get value out of its money.

Advertising and marketing restrictions exist in a number of countries.

France and Italy impose restrictions on the use of computerized reservations systems. Germany has also imposed such restrictions, but most have been removed.

A number of countries have fly-national practices that are far more restrictive than those of the United States.

Staff members of this Subcommittee were contacted by representatives of some foreign airlines alleging that they likewise experienced discriminatory practices in the United States. These representatives were invited to appear at our hearings in order that we may receive additional information to remedy those situations. They declined the offer.

One reason for a large variation in charges between the United States and foreign countries is that foreign countries try to recover full costs of certain services whereas the United States does not. For instance, the U.S. air navigation system is defrayed by a combination of general tax revenues and aviation taxes such as the excise tax on tickets, whereas foreign governments may recover full costs, including investment. The landing fees and terminal navigation charges at European airports are included in airport charges.

Since passage of IATCA in 1979, only three formal complaints have been filed, as provided for in the Act. As of the date of our hearings, two of these complaints have been resolved to the satisfaction of the carriers. (One resolved complaint involved Japan's restrictions on Air Micronesia's service beween Guam/Saipan and Japan, which benefited Japan airlines. The other involved Germany's restriction on TWA's ability to offer competitive fares between the United States and Germany, which benefited Lufthansa.) The third formal complaint was still under consideration. In that case, United Airlines asserted that Japan's CAB was in violation of the bilateral agreement between the United States and Japan when it denied the airline authority to provide service between Seattle/Portland and Tokyo.

Data collected by GAO indicated that most complaints are initiated by carriers in an "informal" manner, through letters and conversations with U.S. Government officials and/or the foreign carriers and their governments. Representatives of the major U.S. international air carriers testifying before this Subcommittee expressed a need for a more active, forceful stance on the part of the U.S. Government which would reduce the need for self-help by the carriers—and reduce the risk of retaliatory action by the foreign governments. Reprisals, they stated, are both blatant and indirect. A government-owned or government-backed carrier, for instance, which owns the airport, reservation system, fuel trucks, groundhandling system, and has the power to set operational restrictions on an American carrier has many opportunities to retaliate either against the airline filing the complaint or another U.S. carrier operating in the country. If the U.S. Government takes action on a government-to-government basis by taking a position on behalf of all U.S. carriers, such action should carry weight. The CAB, it turns out, does not maintain systematic records of informal complaints, action taken, or resolution.

U.S. airline representatives felt that the policy stated in IATCA—which is designed to secure for U.S. air carriers a free and fair marketplace abroad—should be reaffirmed by the Congress and the CAB should be directed to enforce the law. Elimination of discriminatory and unfair practices should become a top priority in negotiations. If negotiations are not fruitful in eliminating such practices, the CAB should invoke its statutory authority by initiating formal proceedings against the airline of the offending country. If the CAB did this on its own, the foreign government would have more difficulty retaliating against individual U.S. carriers. The airline representatives stated that existing discretionary remedies have not worked. Congress should amend IATCA to ensure that government officials respond promptly and forcibly.

The views expressed by representatives of the current and past administrations were, understandably, less emphatic than those of the airline officials.

Marvin Cohen stated his belief that discriminatory problems are neither new nor a product of the liberal aviation policies, but the cost of doing business in an international market. CAB's activities on behalf of U.S. carriers are continuous, informal, and low profile. It needs formal complaints from the carriers, however. The CAB does not have the information or the resources to track down and verify cases of discriminatory practices on its own, and, by initiating action on its own, the CAB may actually hurt rather than help carriers. Agreeing with the airline representatives, Mr. Cohen recommended that IATCA should be revised, making it clear that CAB's powers to take retaliatory actions are not limited to permits and tariffs.

Dan McKinnon believed that we generally need to advance our goals through negotiations. Sanctions, he felt, must be used sparingly. If we use retaliatory sanctions or trade restrictions, we may suffer retaliation.

Judith Connor stated that freeing U.S. airlines completely from interference by foreign governments is in practice unattainable. Such practices are not easily eradicated, but must be pursued diligently. The government should act firmly whenever consultations fail.

Robert Hormats was aware of the concerns expressed by the U.S. carriers—that the government has not been as assertive or protective as it should have been in protecting their rights abroad.

III. Findings

Problems encountered by the airlines were perhaps less important in the past because other countries pursued essentially the same aviation policies. Our policy has differed substantially in recent years, and some observers assert that these policy changes sparked operational conflicts. Invoking retaliatory methods are complicated, however. When the government takes action, we must be sure that the action reflects the concerns of different interests: the carrier filing the complaint, other carriers that might be affected, the traveling public, shippers, unions, etc. Experience has shown that we have historically negotiated hard rights for soft rights. That is, we have been giving up routes and schedules of greater economic value than we have been getting—in the interest of lower fares and new airline entrants.

We have not involved our airlines in negotiations to the extent that foreign countries have involved theirs. We have not developed the cadre of air transportation experts that many countries have. In short, we have often not bargained as forcefully and effectively for our airline interests as we should have.

We have not involved U.S. airport operators in bilateral negotiations to the dimensions which the subcommittee believes they should be. In 1977, the Airport Operators Council International, which represents airports that enplaned just about all of the U.S. international scheduled airline passengers and cargo traffic, presented undisputed testimony on their exclusion from these discussions to the Aviation Subcommittee of the Committee on Public Works and Transportation,

when that subcommittee was conducting public hearings on United States International Aviation Negotiations.

Subsequent to those hearings, and other public hearings conducted by the United States Senate Aviation Subcommittee, Public Law 96–192, the International Air Transportation Competition Act of 1979, amended the Federal Aviation Act of 1958 by adding new subsection (c) which provides:

CONSULTATION WITH AFFECTED GROUPS

> (c) To assist in developing and implementing such an international aviation negotiating policy, the Secretaries of State and Transportation and the Civil Aeronautics Board shall consult, to the maximum extent practicable, with the Secretary of Commerce, the Secretary of Defense, airport operators, scheduled air carriers, charter air carriers, airline labor, consumer interest groups, travel agents and tour organizers, and other groups, institutions, and government agencies affected by international aviation policy concerning both broad policy goals and individual negotiations.

The subcommittee did not believe it was essential to develop additional testimony during these hearings on this point since it was clear nothing had transpired to change the real world climate which had been adequately presented to the Aviation Subcommittee in 1977.

We do believe it noteworthy to repeat that the aforementioned IATCA legislation required that parties affected by Civil Air negotiations be consulted to the maximum extent practicable. Considering the controversial problems of airside and ground congestions, noise constraints, user charges and contract arrangements, all of which have become high visibility issues in recent negotiations, we consider the failure to allow the airport operators greater participation in negotiations where such issues are discussed, to be unwise and an unwarranted exclusion of community concerns. Generally these matters are their immediate responsibility and the economic stakes involved justify their participation, as well as that of consumer representatives who ultimately end up paying for any increased costs.

Our most obvious and most fully documented deficiency is in our failure to respond forcefully to foreign discriminatory and unfair competitive practices. As a result, there is not a fair and equitable market for our carriers in international transport. Airlines often pay higher prices for fuel. They often pay excessive user charges for landing fees, navigational fees, and comparable services that are either free or cost foreign airlines much less in the United States. They are denied full access to computerized reservation systems in some countries. They must use inefficient and indigenous groundhandling crews in some countries. In several Asian countries, they can't get their revenues converted from foreign currency to U.S. currency in a reasonable period of time. There are many more such problems, but our government has handled only three formal complaints. Any new U.S. airline entering the international market will face such problems. The Act is clear that such discriminatory practices are not to be condoned and that our government is to develop firm policies to deal with them—including taking action against the other country's airline if such

problems persist. This Subcommittee believes that a much firmer implementation of the Act is needed.

Our airlines are competitive and efficient, but generally they are competing against the authority and financial strength of foreign governments that want their airlines to succeed for a variety of nationalistic reasons in addition to transportation. Even the United States helps foreign carriers indirectly through its support to the Export-Import Bank which provides low interest rate loans to foreign carriers to enable them to purchase new equipment. In many countries, the total airline infrastructure—airports, reservation systems, travel agencies, and groundhandling—are controlled and sometimes owned or subsidized by the government. U.S. privately owned carriers must compete with these national protections, subsidies, and monopolies in order to survive—with no backup from our government.

The IATA has been a multilateral forum for establishing airline fare structures for many years. Although it has limitations, it still has the strengths of airline involvement in a multilateral forum to develop fare schedules subject to approval by the governments involved. The CAB show-cause order and the open skies policies have seriously undermined IATA and possibly caused the airlines and foreign governments to pursue nationalistic policies with respect to the United States—such as escalation of unfair and discriminatory practices.

IV. Conclusions and Recommendations

This Subcommittee's extensive hearings on the United States international air policies—nine days over eleven months with testimony from numerous witnesses—have supported and reinforced the principles established by the International Air Transportation Competition Act. This Act calls for an international air policy that balances air carrier economic viability against consumer interests in lower fares and quality service within the context of an international market free from unfair and discriminatory practices.

Our hearings conclude that the implementation of this Act by the Executive Branch fails to achieve IATCA goals in several important respects. Our carriers' economic viability has been adversely affected by an Open Skies policy which has extended domestic deregulation to the international arena. The policy extension fails to recognize the traditional relationships among countries and the contribution of international transportation organizations.

Our agencies—CAB, DOT, and State—have not forcefully negotiated bilateral agreements that support our air industry because they have failed to:

develop a professional staff with an adequate air transportation capability;

maintain a consistency among negotiators and administrators;

establish a dialogue with our air carriers and consider their problems;

adequately coordinate negotiations among the three agencies; and assign permanent leadership to a high level position.

These weaknesses have contributed to a long-existing pattern of unfair/discriminatory practices by other governments against our flag

carriers that include excessive charges for landing, fuel, and navigation; problems with baggage handling and reservation systems; airport service restrictions on flight frequencies; and difficulties in getting bilateral arrangements implemented.

Our Executive Branch agencies are currently beginning to acknowledge the contribution of international air transportation to tourism, balance of payments, defense readiness, and a comprehensive trade policy for services. Some positive actions have been taken since these hearings began. One important action is the recent European Civil Aviation Conference agreement which represents, for the first time, a multilateral approach to liberalizing air fares within zones of reasonableness. Reportedly, the U.S. Trade Representative is making progress in developing an international services policy of which air transportation is a part. Some progress is also being made in negotiations leading to elimination of unfair/discriminatory practices, including freezing charges at Heathrow Airport pending results of a cost study to be completed in May 1983; satisfactory access by TWA to Germany's reservation system; progress toward using U.S. carrier personnel for ground operations in Italy; interim agreement with Japan permitting United Airlines to initiate service; elimination of a fuel tax in Canada and refund of taxes paid; and agreement to allow American Airlines and Flying Tigers to begin service to Brazil. We also detect a hardening of bargaining positions by our negotiators, including an increasing unwillingness to trade hard rights for soft rights.

This Subcommittee recommends that the Executive Branch develop and implement an international air policy that carries out the original intent of IATCA. Despite the recent improvements noted above, major reforms are necessary in order to provide a fair market environment for our flag carriers. It is clear that a much firmer position needs to be taken in international negotiations to insure that discriminatory practices are eliminated and valuable economic routes are not traded away. Our examination of the issues demonstrates that the agencies must improve the negotiation process through earlier and more intensive involvement of our flag carriers, improved agency technical capability, continuity of personnel and policy over time, and closer interagency coordination. We reiterate the recommendations of the Congress as set forth in IATCA calling for consultation to the maximum extent possible with airport operators and consumer interest groups. The Administration needs to develop a more encompassing international air policy that reflects broader national goals. U.S. policy should not place any U.S. air carrier at a disadvantage. While we should negotiate for a liberal policy, we cannot permit continuance of a unilateral policy where the other parties to the agreement cannot be and will not be coerced into changing their policies into free access policies.

The administration should make it clear to other countries, our flag carriers, and even to our citizens exactly what they should expect from U.S. international air policy. Specifically:

We will not tolerate discrimination.

We will not trade hard rights for soft rights.

We will not negotiate aviation rights for benefits in other economic sectors.

We will continue to seek flexible air fares within zones of reasonableness.

We will return to active participation in IATA and other international forums.

We will continue to seek multilateral agreements.

We will actively seek to identify excess user charges and fees, and insist on their elimination.

We will develop an information system which identifies both formal and informal carrier complaints about discriminatory/unfair practices, and follow-up on the disposition of such complaints.

We will improve our capabilities and policies for negotiations.

We will follow up on bilateral agreements to insure that the terms are implemented by foreign governments.

In short, we want to insure that there is a fair and equitable market environment for international air travel that provides for profitability for our flag carriers, reasonable rates and quality service for our consumers, and a consistent and firm position to present to foreign governments and their carriers. This would be a policy of which we could be proud and one this Subcommittee hopes will be well established by the time we return to this arena for an assessment of how these recommendations have been implemented.

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